

FACTORS AFFECTING SMEs SUCCESSFUL UTILIZATION OF TAX INCENTIVES IN MANUFACTURING SECTORS

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Abstract

This study aimed to determine the key factors associated with successful utilization of tax incentive and to further investigate which factors were significant via the logistic approach. Using the convenient sampling, 125 SMEs in the manufacturing sector were selected as samples. The findings showed four factors; capital investment, business strategies, government support and environment were significant in attributing to successful utilization of tax incentives. A further analysis using the logistic approach was extended to determine the underlying factors of why some SMEs were able to utilize the tax incentives, whilst others were not. The results from the logistic approach revealed that factors related to the governance of companies had significant influence on the ability of the company to effectively utilize the tax incentives. This study used both primary and secondary data and employed methods, such as, survey and real financial data analysis retrieved from companies' financial statements.

Keywords: *Tax incentives, utilization of tax incentives, successful, SMEs, manufacturing sector, economic goal.*

Introduction

Small and Medium Enterprises (SMEs) play a pivotal role in the overall performance of the country's economic development. Its existence is increasingly important as the backbone of the national economic development in both developed and developing countries (Ayele, 2006; Loo, 2000; McKenzie and Sakho, 2010; Saleh and Ndubisi, 2006). The 2003 Malaysia Census of Establishment and Enterprises reported that SMEs accounted for 99.2% of 552,804 business establishments, providing 5.6 million jobs of which comprised 56% of the total employment in Malaysia (SMIDP, 2005) and contributing about 32% of the country's gross domestic product (GDP). Considering the importance of SMEs' contribution towards nation development, government continuously crafts various fiscal and non-fiscal incentives support programs to foster growth within SMEs. Previous studies highlighted the diverse purposes of these incentives, served to match the intended objectives set by the governments of particular countries. In developed countries, tax incentive has been used as a tool in reducing unemployment, promoting specific economic sectors or attracting companies towards certain types of activities. On the contrary, developing countries have frequently used tax incentives to attract Foreign Direct Investment (FDI) into their countries (Zee, Stotsky and Ley, 2002). Although each type of fiscal incentives serves different purposes, the *modus operandi* of tax incentives are similar where companies are allowed tax exemption which ultimately leads to a reduction in their tax liability (Ayele, 2006; Ihlanfeldt and Sjoquist, 2001; Jomo, 2007; Morgan, 1987).

Unfortunately, several studies claim that tax incentive is ineffective and has departed from its fundamental purpose of reducing tax liability and stimulating the SMEs' investment project (Jomo, 2007; Mackay, 1994; Moha, 1999; Rasiah, 1996; Rasiah and Shari, 2001). Tax incentives are found to be weak policy instruments either in attracting entrepreneurs to set up their businesses within the promoted areas or in appealing entrepreneurs into the industries promoted by the special tax exemption. Furthermore, studies found that tax incentives favored large business organization which are influential enough to draw the attention of certain political interest (Rondinelli and Burpitt, 2000). While previous studies reported on the ineffectiveness of these incentives in stimulating the investment project for SMEs, few empirical research have examined the common factors associated with successful utilization of the tax incentives among SMEs (Mydin and Abdul Rahim, 2003; Rondinelli and Burpitt, 2000). Thus, focusing on the Malaysia scenario, this study intends to achieve two objectives. First, to determine factors associated with successful utilization of tax incentives and second, to assess the key factors which might impact on the SMEs successful utilization of tax incentives. This study is crucial because lack of research on tax incentives restraint SMEs from being well informed and updated on the benefits of tax incentives. In addition, the findings of this study would enrich the data base of successful SMEs in utilization of tax incentives and thus, they can be modeled as successful leaders among SMEs (Ihlanfeldt and Sjoquist, 2001). As stated by Kennell (1995), small firms are not motivated by large firms' experiences due to different in sizes. He argues that small firms need sector champions who will disseminate information on tax benefits, share their success knowledge and become role models in the industry.

The call for re-examination of tax incentives utilization necessitates an analysis of both the financial statements of the companies and data on internal and external factors (Kuo and Li, 2003) which may have significant impact on the performance of SMEs. In this study, the discussion on tax incentives was limited to SMEs in the manufacturing sector. The motivation of analyzing this sector was associated to differences in the unit labour cost of the manufacturing sector which was higher than large firms. The manufacturing sector reported a unit labour cost of RM0.07, while SMEs in general reported at RM0.08, and large firms declared a unit labour cost of RM0.06 (SMIDEC, 2002). Hence, these tax incentives initiated by the government are timely as they will help the SMEs in the manufacturing sector to be more competitive and able to reduce their cost of doing business in the long run. This result will enable both the policymaker and SMEs to re-evaluate the relevance of tax incentives, in terms of their appropriateness in achieving the targeted productivity level and their effectiveness in enhancing competitive advantage (IMP, 1994).

Subsequently, the following section presents the relevant literature in tax incentives up to date. Section three highlights the sample selection technique and methodology. Section four discusses the analysis of data and in this section questionnaires were used to solicit respondents' perception on how to determine the underlying factors in measuring SMEs successful utilization of tax incentives. To obtain the actual result of whether SMEs were able to utilize the granted tax incentives or otherwise, the amount transferred to the tax exempt income account were analyzed in their five years financial statements. By using Logistic Regressions, the study then further identified factors which were able to explain why some SMEs utilized their tax incentives while some did not. Finally, Section five concludes with recommendations for future research undertakings.

Literature Review

In developing countries, extending tax incentives to encourage FDI has been an important economic instrument since 1990s (Hadari, 1990; IMP3, 2006; Rolfe, Ricks, Pointer and McCarthy, 1993; Zee et al., 2002). These countries are looking at the positive impact gained through FDI, most importantly, FDI not only induces investment in favor of certain industries, generates employment in domestic labor market but also transfers technology and managerial know-how to stimulate growth of economically lagging regions (Rondinelli and Burpitt, 2000). On the contrary, Hadari (1990) claims that foreign decision to invest abroad is not directly influenced by attractive investment tax incentives. There are other more important factors in attracting FDI to developing countries, such as sufficient economic infrastructures, stable political regime, low labor cost and less bureaucratic administration. Hence, in reality the decision to invest abroad is made way before looking at the availability of tax incentives.

Apart from attracting FDI, previous studies also reveal on the effect of tax incentives on the investment policies of the companies. Conducting a survey on a large sample of firms in the manufacturing industry in United Kingdom, Alam and Stafford (1985) confirmed that, taxation and tax incentives were not the major factors influencing investment decision.

Although taxation does not appear to be a major factor in companies' project appraisal involving investment decisions, it does emerge as a subordinate (secondary) element in a complex decision making process. In conclusion, when evaluating the effectiveness of tax incentives, its importance on companies cannot be judged in isolation. The benefit of tax incentives as an appealing investment tool should be parallel with other economic support, for example, good physical infrastructure, availability of site and premises, political factors and others (Ayele, 2006). Tax incentives are important investment stimulant for SMEs and Radulescu and Nam (2006) claim SMEs are generally more responsive than larger corporations towards domestic tax incentives. This is because tax can play an important role in the cost structure of SMEs since they do not have the financial and human capacity to develop sophisticated tax avoidance¹ strategies. Therefore, by obtaining tax incentives; it helps to reduce their production cost, exempt from income tax liability and thus increase their net financial benefits. Bolton (1971) in Poutziouris et al. (2000) quoted the importance of the economic and taxation system of a country in enabling individuals or business entities to preserve the small firms sector. Given the appropriate tax structure and other favorable economic conditions which are directed to influence the performance of SMEs, the positive impact is likely to be huge and holistic for the country in general.

Furthermore, small businesses are consistently facing numerous challenges in their attempt to progress from micro businesses into larger entities, with limited source of fund as the major constraint. Observing the plights of SMEs, the government is strongly motivated to extend aid in terms of tax incentives to SMEs. The presence of this tax incentives policy serves as a purpose to encourage growth of SMEs, and improve its value added and productivity. Ultimately, all these combined supports will be the catalysts to allow them to penetrate the international market and contribute to the overall economic well being of the country.

Tax Incentives and SMEs

At the operational level, it is difficult to measure and evaluate small business programs and policies's success. As pointed by Storey (1994), many policies have been designed to cater to the needs of SMEs and these policies are being introduced on a piecemeal basis and are often poorly specified. Objectives are stated but in 'politician words' and polices are frequently quoted as a tool to enhance key management skills in the entrepreneurial firms. Persistently, these words are 'lip-service' or a political instrument of popularity and media savvy (Ghazali and Alias, 2001). Thus, the main problem within the policy measures is to determine whether these policies are feasible and achievable in ensuring the success of meeting the targeted objectives of SMEs.

However, to measure the successful performance of the SMEs is not only by looking at the achievement of the government's targeted policy but it depends on numerous factors, both internal and external to the companies. Among them, abilities and other personality traits of those who manage the companies are regarded as the most powerful set of factors

having either positive or negative impact on SMEs performance and success (Curran, 2000). Storey (1994) in his review of past studies identifies three factors influencing decision to set up new ventures which are:

- a. Personality
- b. Human capital
- c. Ethnic origin

Personality traits of individuals managing the enterprises become a central topic of interest among economic psychologists, such as, Chell, Haworth and Brearly (1991). According to these authors, entrepreneurs who are attentive to business opportunities are those who are proactive rather than reactive, innovative rather than easily bored. Other personality traits related to success factors in the performance of SMEs are personal initiative, competent SMEs owner/manager and availability of government support programs (Che Rose, Kumar and Yen, 2006). The authors find that among the Malaysian entrepreneurs, personal initiative is acknowledged as the key element in contributing to the success of SMEs. This characteristic is important because entrepreneurs with high personal initiative are able to overcome their own weaknesses through proactive attitudes. In addition, high personal initiative acts as a strong motivation to entrepreneurs to further enhance their management talents, improve business operation skills and embark into life-long learning attitude. These attributes are derived from entrepreneurs' education level, working experience and family business inheritance which overtime would likely secure their successful performance in business. Many studies indicate that the educational level of the SMEs owner/manager is an important factor in developing the entrepreneur's managerial skills and personality (Ibrahim and Goodwin, 1986; Rose, Kumar and Yen, 2006; Shahadan, 2001). Hence, as the company grows, the SMEs owners/managers must be able to: promote and advertise their products and services, understand market needs and attend customer feedback. Knowing the trends and accurately forecasting the future will allow a longer period of business survival.

Ayele (2006) claims that other push factors related to the environment, such as, employment, location of the promoted area and the policy time lag are important in influencing decision made by the SMEs owners. According to Pfeffer (1972), the board of directors can act as liason in dealing with the organization's external environment. He identified two distinct strategies for the company's survival and growth. The first strategy is to concentrate on improving the efficiency of the internal transformation process which will optimize the resources and expand business transaction. The second strategy is to improve favorable exchanges with external organizations through political influence. Both strategies are achievable if the board is able to play their role in maintaining internal efficiency and engaging into a long-term contract of supplying their product through the interlocking board of directors. The company will be at an advantage if the board members are influential figures from leading business associations or directly linked to certain political affiliation (Ghazali and Alias, 2001).

Sample Selection and Research Methods

Samples for this study were drawn from the MIDA's list of SMEs applying for tax incentives and out of 200 SMEs selected, 125 SMEs met the specified criteria. The questionnaires survey in this study provides data on trends of the factors influencing SMEs successful utilization of tax incentives. The structure and issues covered in the questionnaires were drawn from the literature review (Ayele, 2006; Che Rose et al., 2006). The 41 final total useful respondents were found statistically adequate and acceptable (Sekaran, 2000). The financial statements (Piotroski, 2000) of the 41 respondents were also extracted from CCM to obtain their financial data during tax relief period. Factor analysis was applied to trace the existence of the principal components and any insignificant variables found were eliminated. Referring to Dess and Davis (1984) as quoted in Ibrahim and Goodwin (1986), factor analysis is able to produce descriptive summaries of data matrices, which can aid in detecting the presence of meaningful patterns among a set of variables. However, prior to factor analysis, Cronbach alpha coefficients were calculated to measure the reliability of the statements in each dimension of the questions.

Findings

The following section presents the findings of this study.

Results of Factor Analysis

The categorized statements used to measure perceptions of respondents had to be consistent and reliable. The Cronbach alpha (Nunnally, 1978) values for all dimensions ranged from 0.768 to 0.900. The figures indicate that the statements are reliable measures of the respondents' perceptions on the categorized five dimensions. The selected samples were then assessed for their suitability to factor analysis. Inspection of the correlation matrix revealed the presence of coefficients of 0.3 and above. Bartlett's Test of Sphericity was highly significant ($p < .000$) and the Kaiser-Meyer-Olkin (KMO) measure of adequacy gave a value of 0.636. Principal components analysis yielded six significant factors from five dimensions with eigenvalues exceeding 1 which explained 37.80%, 13.12%, 8.85%, 6.96%, 6.37%, 5.68% of the total variance respectively. Six components were generated in this process and the distribution of statements in Component 1 to 3 were found to be optimum but the distribution of items loading on Components 4 to 6 were not optimal and inappropriate since only few items were loaded in each components. Thus, this study decided to retain only four-factor solutions to ensure results were appropriate and optimum. PCA with varimax rotation was repeated with four-factor solutions and the results in descending order loading were presented in Table 1.

These four-factors were then labeled as: capital investment, business strategies, government support and environment (external relationship). Most of the items loaded strongly (above 0.40) for each of the factors. According to Ibrahim and Goodwin (1986), in order to be included in any particular component, each success factors must exceed a factor loading of 0.60 on one factor and not load at more than 0.40 on any of the other

factors. They mentioned the purpose of specifying these criteria which was to minimize the uncertainty related in separating the different factors. Low value of factor loading, for example, any value less than 0.30 could indicate that the item does not fit well with the other items in its component (Pallant, 2007). Thus, in this study, it was decided that the success factor loading needed to be more than 0.40 on one factor and not load at less than 0.40 on any of other factors.

Table 1: Key Factors in Determining Successful Utilization of Tax Incentives of SMEs in Manufacturing Sectors

Factor 1 Capital Investment		Factor 2 Business Strategies	
Item	Loading	Item	Loading
Machinery and Equipment	.822	Product diversification	.867
Production increase	.785	Market expansion	.752
Sufficient cash in hand	.775	Competency of top management	.619
Automated manufacturing	.730	Domestic competitors	.603
Profit increase	.710	Penetration global market	.530
Sales turnover increase	.662		
Factor 3 Government Support		Factor 4 Environment	
Item	Loading	Item	Loading
Reduce tax liability	.905	Subcontract with other companies	.731
Role of government agencies	.727	Networking	.713
Government support program	.697	Other successful SMEs	.680
Promotion by MIDA	.619	Support from SME Corp	.621
Professional assistance from MIDA	.548	Pre and Post monitoring from MIDA	.487
Industrial linkage	.498		

Factor 1: Capital Investment

This factor contributed about 37.78% of the total variance explained and was ranked as the first factor. The variables loaded in factor 1 were the investment taken by top management when the companies were profitable, hence allowing the utilization of saving from tax exemption derived from tax incentives. In this study, the respondents labeled capital investment as the main criteria in predicting successful utilization of tax incentives. Investment in more advanced machinery and equipment and use of automated manufacturing process would lead to increase in productivity level which allows companies to meet increasing demand. Ultimately, the increase in demand will boost sales turnover and increase level of profitability in terms of retained earnings and cash flow.

Factor 2: Business Strategies

This second factor contributed about 13.12% of the total variance explained. Business strategies were the key elements for any organizational success designed by the top

management in the attempt to ensure survival and sustained growth. Hence, strategizing is important to SMEs and they must ensure that their companies are able to secure profitable investment projects continuously. In this study, the respondents' perceived strategies such as product diversification, market expansion, top management commitment, and enhanced competitiveness were among important business approaches that should be implemented by SMEs.

Factor 3: Government Support

This factor accounted for 8.85% of the total variance explained. In this category, the factors included were: reduction in tax liability, roles of government agencies in promoting the support programs to SMEs, promotional effort by MIDA to encourage other eligible SMEs to apply for tax incentives and professional assistance by MIDA to simplify the tax incentives application process and promote industrial linkages among SMEs and with other large business organization.

Factor 4: Environment

Other than government factors, this study also emphasizes the important function of environment related to external relationship. Those factors include giving subcontracts to other companies, developing networking, following the path of successful SMEs, making close relationship with SME Corporation and having access to government agencies' monitoring report.

The findings of this study to some extent have contributed to the literature by providing empirical evidence that capital investment, business strategies, environmental factors and external relationship are among the crucial factors perceived to contribute towards SMEs success in utilizing tax incentives. These factors can be used as criteria or guidelines for the policymaker and SMEs in evaluating the relevancy of tax incentives not only to the company's performance but also towards the general economic performance of the nation. After determining the key factors in the perceptions of the respondents as to what are the important variables in successful utilization of tax incentives, the study then further identified factors promoting SMEs to utilize or otherwise the tax incentives during their tax relief period. These factors were found to have critical impact on the utilization of tax incentives. The factor analysis showed that the factor of the firm's characteristics had greater influence on its success in utilizing tax incentives as compared to other factors. Further inferential statistics, such as, Logistic Regression was applied to identify which of the factors were significant in contributing to successful or unsuccessful utilization of tax incentives.

Logistic Regression Model

Findings

A survey was conducted to analyse the factors to differentiate between successful SMEs in utilization of tax incentives against those who were not. In this analysis, the term 'successful' and 'unsuccessful' utilization of tax incentives refers to SMEs which are

able to transfer the amount of tax exemption profit derived from tax incentives to a pool of fund in the company which can be utilized later. This pool of fund is known as the tax exempt income account which is observable from the annual financial statement of the company. The cross examination of data using the direct logistic regression was used to determine the relationship between the dichotomous dependent variable (Ihlanfeldt and Sjoquist, 2001) and thirteen other independent variables as listed in Table 2 (Refer Appendix). The model as a whole explained between 59.5% (Cox and Snell R square) and 79.4% (Nagelkerke R squared) the variance on SMEs utilization of tax incentives.

As shown in Table 2, from the thirteen independent variables, only six were statistically significant. Those variables were: profit, board size, ethnicity of the board members, board members' political affiliation, date of tax incentives granted and education level of the SMEs owner/manager which are significant. On the other hand, this study found that working experience, type of industry, assistance from government agency (MIDA), selection of auditors, type of tax incentive, date of incorporation and location were not significant. The Chi-Square value for the Hosmer-Lemeshow Test was 2.498 which was significant at 0.962, a value larger than the 0.05, indicating that the result strongly supported this model (Pallant, 2007).

Table 2: Logistic Regression Predicting Likelihood of SMEs Utilization with Tax Incentives

Independent Variables	B	S.E.	Wald	df	Sig.
Profit	4.368	1.994	4.799	1	.028
Board of Director (Board Size)	1.805	.795	5.151	1	.023
Board of Director (Ethnicity)	1.681	.782	4.622	1	.032
Political Affiliate	-6.066	3.035	3.995	1	.046
Date of Tax Incentive	5.488	2.435	5.080	1	.024
Education	5.738	2.683	4.574	1	.032
Working Experience	-2.453	3.853	.405	1	.524
Type of Industry	-.224	.201	1.242	1	.265
Professional Assistance	1.822	1.675	1.182	1	.277
Auditor	3.790	3.242	1.367	1	.242
Type of Incentive	.440	.340	1.674	1	.196
Date of Incorporation	1.171	1.504	.606	1	.436
Location	.438	2.066	.045	1	.832
-2 Log-likelihood	19.583				
Model Chi-Square	2.498				
Hosmer and Lemeshow (Sig.)	.962				
Cox and Snell R Square	0.595				

Discussion

The empirical evidence in this study reveals that generally the significant factors discussed above can satisfactorily explain why some SMEs are able to utilize the tax incentives while others are not. These success factors are generally associated to all elements of the company's governance characteristics which are related to the resilient board members' attitudes in overcoming any perceived or actual events that may likely impact the company's performance. Following this finding, it is useful to discuss some distinct governance characteristics to indicate their importance in the companies' success of utilizing tax incentives.

Governance Characteristics

Among the five independent variables related to governance characteristics: board size, ethnicity of board members, board members political affiliation, professional assistance from government agency and selection of auditors, only three of these variables show significant relationship with the SMEs's success in the utilization of tax incentives. The strongest predictor is the board size, which can be interpreted as the larger the size of the board, the more effective the role of the board as a leader of the company which has been granted incentives from the government. Although, past studies debated on the effectiveness of having larger board size which could often create greater agency problems (Hermalin and Weisbach, 2003), small boards tend to lack the advantage of having the spread of expert advice and opinion during meetings which are often found in larger companies. On the other hand, in support of larger board size, some proponents claim that a large board is able to contribute in terms of experience, skills (Dalton and Dalton, 2005) and business networking (Sherer, 2003) which are crucially important for SMEs to survive and further improve the company's performance (Larmou and Vafeas, 2010).

Another important governance characteristic which determines the successful utilization of tax incentives is related to the ethnicity of the board members where such a situation is not unusual in a multi racial country like Malaysia. Past studies related the heterogeneity of board members to their cultural values that influenced their business conduct, information seeking behavior and family involvement. Furthermore, the presence of multi-ethnics board members in the administration of the company will improve regulation compliance, increase transparency, enhance accountability and promote independence (Basu, 1998; Marimuthu and Kolandaisamy, 2009). Although this study did not provide strong evidence on the direct relevancy of the board members multi-ethnics and SMEs successful utilization of tax incentives, the existence of such element did support the cultural theories which had some influence on companies' work ethics and their ability to develop external relationship that eventually reduced uncertainties in their business environment (Basu, 1998; Marimuthu and Kolandaisamy, 2009).

Political affiliation is also an important feature of governance characteristic leading to successful utilization of tax incentives. The result showed that the increase in number of political affiliation among board members would less likely cause unsuccessful utilization of tax incentives. In other words, the existence of the board members with important political affiliation offers greater opportunity to the company in securing

projects through their political linkages in the process of lobbying for the investment project (Lambsdorff, 2001). The lobbying of investment project becomes intense due to stiff competition among several interested parties. This situation is attributed to the fact that policies are formulated by politicians at ministerial level who have vested interest to help cronies around them (Faux, 1971; Ghazali and Alias, 2001). This scenario enhances political backup and supports among politicians and business community in good times and bad times (Ariff and Abu Bakar, 2002). The political affiliation of board members can serve as a media of communication with politicians in any event that back-ups are needed in the business.

Logically, the lesser the time taken to approve tax incentives for SMEs, the faster the utilization of the tax incentives can be undertaken. Indirectly, it means that, if those SMEs have problems completing the application form, this will cause further delay in utilization of tax incentives. However, the issue on utilization of tax incentives is far more critical than facing bureaucracy or red tapes in the course of the application process (Ihlanfeldt and Sjoquist, 2001). Several underlying issues related to monitoring are identified as the contributing factors that inhibit the successful utilization of tax incentives (Ayele, 2006; Ghazali and Alias, 2001; Hon and Chia, 2002; Jomo, 2007; Moha, 1999; Rasiah, 1996). Table 3 tabulates that majority of the SMEs were attracted to Pioneer Status as a popular choice of tax incentives and 23 (56.1%) out of 41 respondents in the survey were granted Pioneer Status.

Table 3: Type of Incentives Granted to SMEs

Type of Incentives	Frequency	Percent
PS	23	56.1
ITA	3	7.3
RA	3	7.3
PS and RA	2	2.4
PS and Tax rate of 20%	8	19.5
ITA and RA	1	2.4
PS and RA and Tax rate of 20%	1	2.4
RA and Tax rate of 20%	1	2.4
Total	41	100

The application process cycle of tax incentives indicates that all application forms related to Pioneer Status or Investment Tax Allowance either from large or SMEs must be submitted to the government agency, MIDA. At MIDA, all the completed application form will be processed within sixty days after the application is received. In cases where incomplete application forms were submitted, the applicants will be asked to resubmit additional information required. According to the survey, from the total of 41 respondents, majority (88.1%) submitted complete application forms in their first submission. The result indicates that there is no barrier or problem in the initial application process and hence, the professional assistance provided by MIDA is not critically essential. Further, the Logistic Regression results in Table 2 show that the assistance from MIDA during the initial application process of tax incentives was not significant.

On the other hand, the education level of SMEs owner/manager (as shown in Figure 1) could be one of the factors contributing to the ability of the applicant to submit a complete application form. From the descriptive finding, majority of the SMEs owners/managers were degree holders (61.9%) and less than 20% of them held secondary school certificate (SPM). Higher education has equipped the SMEs owners/managers with better knowledge and skills (Che Rose et al., 2006) which are crucial towards their business performance. Furthermore, they would have gained some knowledge about tax incentives during their tertiary education and such exposure would have helped them make better choices on the suitability of tax incentives chosen. Besides, educated SMEs owners/managers are more innovative and creative in finding solutions to the problems related to their company's performance (Marcati, Guido and Peluso, 2008) and promote good communicative behavior (Shahadan, 2001) which are essential in establishing linkages with other external factors.

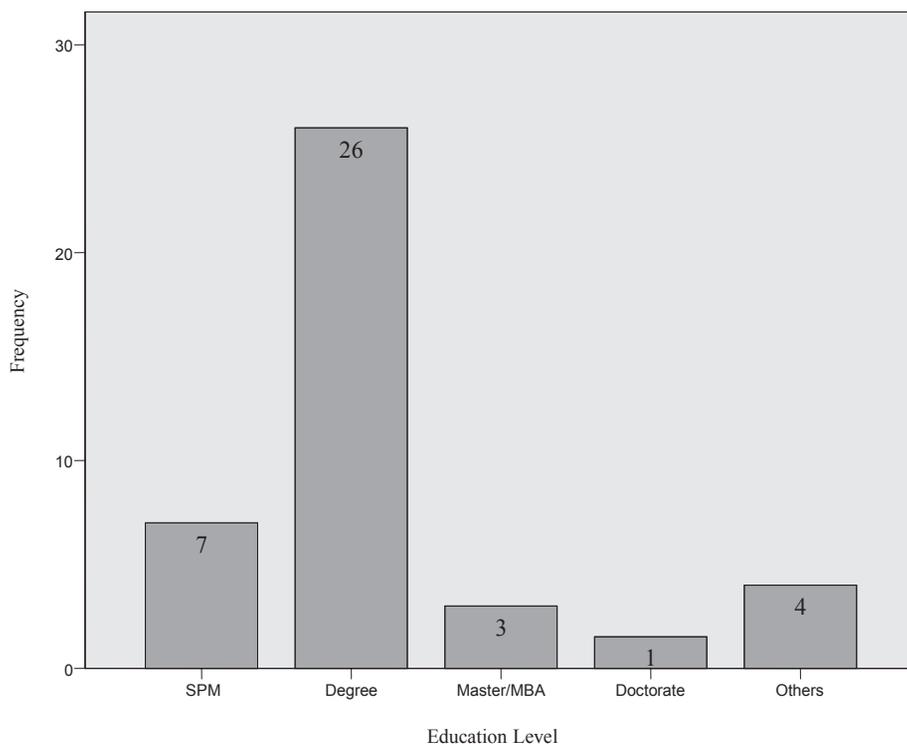


Figure 1: Education Level of the SMEs Owner/Managers

The last independent variable tested in this study, profit, earned during the first year of tax relief period was found to be significant in the utilization of tax incentives granted. However, in cases where companies have unabsorbed losses prior to the first year of tax relief period, the utilization of tax incentive will not take effect immediately because the losses will be off-set against the profit in the first year of tax relief. As a result, the utilization of tax incentives will be delayed and carried forward to subsequent years. In

such a situation, the company was unable to attain maximum benefit of tax incentives immediately.

Conclusions

Overall, this study achieved its aims in determining the crucial factors associated to successful utilization of tax incentives. A distinct conclusion can be drawn from this study which highlights the facts that variables related to governance mechanism are the key factors that further enhance successful utilization of tax incentives. The results highlighted that those SMEs with larger board size are better than those with smaller board size while ethnicity of the board members though do not show direct relationship, it does indicate that its ethnicity has influence on their working culture. The existence of cultural elements in influencing the success of a business is not peculiar but in fact has been proven in other empirical work showing how culture impacted information sharing and securing business opportunity among the same ethnic group (Basu, 2003). Other features, such as, the board members' political affiliation is crucial as a back-up in securing investment projects. The board members' political affiliation gives the SMEs an added value in procuring government contracts within such competitive environment. In addition, the SMEs owner/manager's level of education is important in developing personality and managerial skills. Other significant factors in determining successful utilization of tax incentives include date of tax incentives granted and profit level generated in the first year of tax relief period. On the theoretical and methodological issues, this study provided clear insight towards building a conceptual framework on the determinants of successful utilization of tax incentives. However, there are other avenues for future research where an intense utilization of real data from the financial accounts could be used to determine the appropriate strategy to achieve successful utilization of tax incentives.

Note

¹ Tax avoidance is defined as the legal way of eliminating, minimizing or deferring the payment of income tax, (Kwai Fatt, 2007).

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